

## Market Commentary for August 2009

### Some Positive Signs in August

The lack of volatility in leading economic indicators in August showed further signs that the United States economy is stabilizing. U.S. Gross Domestic Product (GDP) growth for the second quarter of 2009 was negative 1.0 percent, essentially unchanged from the preliminary estimate. While it was a contraction, it was significantly smaller than decreases in GDP in the previous three quarters. It is hoped that the economy will see positive GDP growth in the third quarter of this year, although it may be nominal.

The unemployment rate increased to 9.7 percent in August from 9.4 percent in July. The August figure is the highest since 1983. Aside from health care and education, every sector of the economy shed jobs. Typically unemployment is a lagging indicator and therefore even if the economy has hit bottom, job losses may continue through the rest of the year.

Leading consumer indicators are more or less flat. The Conference Board index of consumer confidence rose slightly in August to 54.1 from 47.4 in July. The expectations component of the index, which measure consumers' attitudes about the future, jumped 10.1 points, while the present conditions component rose 1.6 points. Despite the modest increase, the overall index figure is consistent with a recession. Indeed the University of Michigan consumer sentiment index actually fell marginally in August to 65.7 from 66.0 in July. As with the Conference Board's index, however, the expectations element of the index rose, but the present conditions part fell. It appears that while the consumer outlook regarding the economy is not optimistic, it may be poised for a recovery should other indicators steadily improve. Personal income was flat in July and the saving rate fell to 4.2 percent from 4.5 percent in June. Wage income increased in July for the first time in 2008, although by only 0.1 percent. The core Personal Consumption Expenditures deflator increased 0.1 percent and the core Consumer Price Index rose 0.1 percent.

Indicators were positive for businesses for the most part. Corporate profits rose 5.7 percent in the second quarter with financial corporations leading the way with an increase of 16.7 percent. Retail Sales (MARTS) fell 0.1 percent in

July after two months of solid gains. If autos are excluded, sales dropped 0.6 percent, suggesting that the government's cash for clunkers program had a significant effect on retail sales. New orders for manufactured goods climbed 1.3 percent in July, making for the fourth straight month of increases, while orders for manufactured durable goods jumped 4.9 percent, the largest monthly rise in two years. This latter figure can be attributed largely to a 107.0 percent increase in civilian aircraft orders. Even so, the durable goods orders increase was broad-based. The Institute for Supply Management's manufacturing index, which measures the overall manufacturing situation in the U.S., shot up 4 points to 52.9 in August, breaking the 50 point expansionary threshold for the first time in 19 months. There is cautious optimism that this sector of the economy is recovering.

The housing market is also rebounding, albeit from historical lows. Existing home sales rose 7.2 percent in July, and the rate of sales is back to where it was in the fall of 2007. The median price of an existing home, however, is still down 15 percent on a year-over-year basis. Sales of new homes rose 9.6 percent in July, marking a fourth consecutive month in gains. Like existing home sales, however, the median price for a new home is still down by 11.5 percent year-over-year. In all, the housing market has stabilized and the prospects for recovery look good.

The Federal Open Market Committee met from August 11 to 12 and kept the Fed Funds target rate at zero to 0.25 percent as expected. The minutes from the meeting read, in part, "Information received since the Federal Open Market Committee met in June suggests that economic activity is leveling out. Conditions in financial markets have improved further in recent weeks. Household spending has continued to show signs of stabilizing but remains constrained by ongoing job losses, sluggish income growth, lower housing wealth, and tight credit. Businesses are still cutting back on fixed investment and staffing but are making progress in bringing inventory stocks into better alignment with sales."

### Sector Review





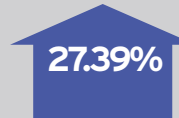

**U.S. Treasuries:** Treasuries experienced some moderate price appreciation during August. A continued reduction in the level of stress on the economy paired by a much better than expected employment report (although still somewhat sobering as job losses continue to pile up) signaled that there may be some economic stabilization in place. Increased supply continues to be well received by the market and auctions are expected to continue at record levels throughout the quarter. The 10-year note yield decreased to a 3.40 percent yield from a 3.48 percent yield over the prior month. The two-year note yield edged downward to a 0.97 percent yield from a 1.11 percent yield while the three-month bill saw yields drop to 0.13 percent from 0.18 percent. (Rates and prices maintain an inverse relationship. Prices decrease as yields increase).

**Commercial Paper:** The London Interbank Offered Rate (LIBOR) dropped during the month as perceived risk continued to recede for financial firms. The unprecedented levels of government support and action taken by financial firms to address liquidity and balance sheet concerns added confidence to the market for deposits and helped contribute to this measured drop. This has benefited issuers whom rely on short-term financings. One-month, top-tier, higher quality asset-backed commercial paper (ABCP) names trade between 0.15 percent and

0.25 percent and three-month paper traded between 0.25 percent and 0.30 percent.

**U.S. Government Agencies:** Agency securities and government backed Federal Deposit Insurance Corporation (FDIC) paper priced at or near levels where comparable Treasury issues have priced in recent months. Investors showed support for these firms on the front-end helping keep yields low in the current historically low Federal Funds Rate environment. Agency yields at month-end on three-month paper yielded near 0.15 percent, six-month paper yielded 0.25 percent, and 12-month paper yielded 0.40 percent.

**Strategy:** The Federal Reserve continues to maintain its Federal Funds target range between 0.00 and 0.25 percent. While there are still some subtle signs of reduced pressure on the economy, slow growth remains evident in the remaining quarters of 2009 (if any positive growth is achieved per estimates of certain Wall Street economists). In this uniquely challenging environment we continue our focus on being highly defensive by attempting to maintain ample cash while trying to be very selective in identifying approved issuers and implementing trade opportunities to add yield when possible.

DJIA		NASDAQ		S&P 500	
	3.53%		1.54%		3.35%
	8.20%		27.39%		12.99%
Month	Year-to-Date	Month	Year-to-Date	Month	Year-to-Date

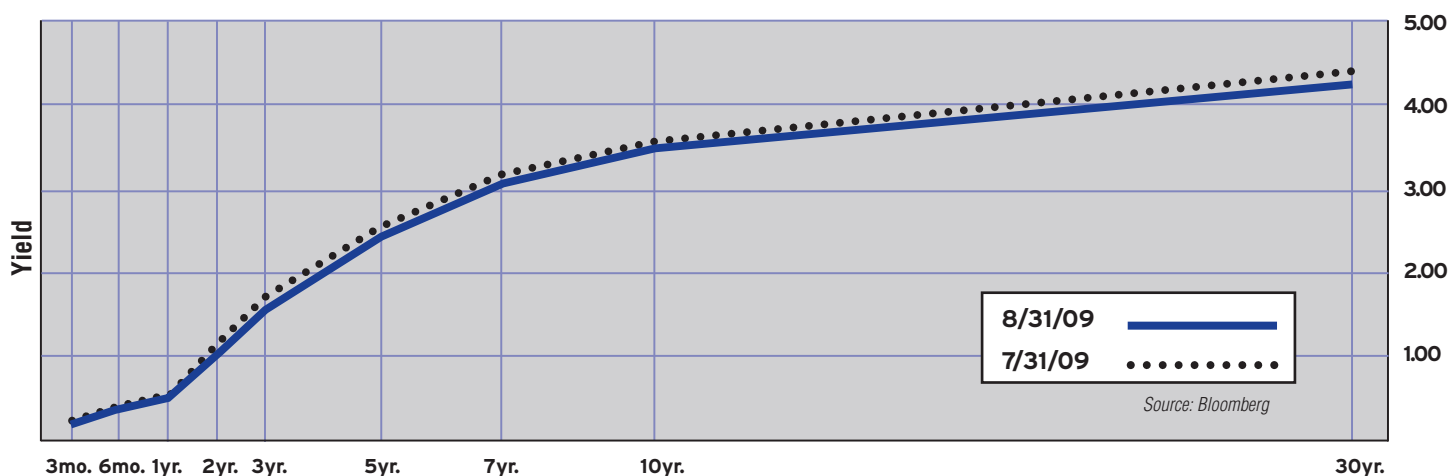
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## Market Summary for August 2009

### Monthly Market Summary - Week-ending Rates and Yields

	08/07	08/14	08/21	08/28	3rd QTR AVG	2nd QTR AVG
<b>Overnight Rates</b>						
Effective Fed Funds	0.17	0.15	0.16	0.14	0.16	0.18
Repurchase Agreements	0.10	0.05	0.10	0.10	0.11	0.14
<b>Discount Rates</b>						
1 Month Treasury Bill	0.13	0.11	0.10	0.08	0.12	0.09
1 Month Agency Disc.	0.15	0.13	0.13	0.12	0.14	0.13
1 Month Com'l Paper	0.25	0.20	0.20	0.23	0.22	0.24
3 Month Treasury Bill	0.17	0.15	0.14	0.13	0.16	0.16
3 Month Agency Disc.	0.19	0.19	0.17	0.17	0.19	0.19
3 Month Com'l Paper	0.36	0.35	0.31	0.27	0.33	0.46
6 Month Treasury Bill	0.25	0.22	0.23	0.21	0.24	0.28
6 Month Agency Disc.	0.30	0.29	0.26	0.25	0.29	0.30
6 Month Com'l Paper	0.47	0.43	0.42	0.39	0.44	0.62
<b>Yields</b>						
1 Year Treasury	0.52	0.44	0.45	0.44	0.47	0.53
1 Year Agency	0.63	0.52	0.56	0.51	0.54	0.73
2 Year Treasury	1.30	1.05	1.09	1.02	1.05	1.02
2 Year Agency	1.47	1.20	1.28	1.15	1.20	1.37
5 Year Treasury	2.82	2.51	2.57	2.45	2.50	2.25
5 Year Agency	3.15	2.91	3.01	2.86	2.91	2.83

### Historical Yield Curve



### Key Economic Indicators

	For the Period	Date of Release	Expected	Actual	Prior
Unemployment Rate	August	09/04	9.5%	9.7%	9.4%
Consumer Price Index	July	08/14	-1.9%	-2.1%	-1.4%
- Less Food and Energy	July	08/14	1.6%	1.5%	1.7%
Consumer Conf. (CB)	August	08/25	47.9	54.1	46.6
FOMC Rate Decision		08/12	0%-0.25%	0%-0.25%	0%-0.25%
Gross Domestic Product	2Q	08/27	-1.5%	-1.0%	-1.0%

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